A NEW STANDARD AND A NEW CURRENCY.

IN 1896 the people refused to sanction a currency policy that, in their opinion, would have resulted in silver monometallism and would have involved injustice to the creditor. May it not be a mistake to assume that this refusal was equivalent to a positive declaration in favor of gold monometallism, or that they would not as decisively reject any currency policy that seems careless of the rights of the debtor? Is it not probable that the policy that receives their positive sanction must not only provide every positive safeguard to the creditor, but must also afford the debtor every practicable facility for meeting his obligations? Such equal regard for the rights of both debtor and creditor is the purpose of the monetary system outlined in this article. An attempt will be made to set forth clearly and simply: (1) those measures intended to improve the media of exchange and facilitate the payment of debts in times of crisis; (2) those intended to provide for the stability of the standard and secure the rights of the creditor; (3) some general advantages to be gained by adopting the system.

I.

The government control of the proposed system will be through an Issue Department, of which the Comptroller of the Currency will be the administrative head. Bank checks constitute more than half of the media of exchange in the United States. It follows that there can be no effective regulation of the means of payment by the government until all demand-deposit banks come under its control. To this end banks that organize under the new national system will be exempt from a tax on demand deposits that will be made high enough to cause all other banks to retire from business.

The deposits in the banks will then be converted into a means of payment, practically legal tender, but much more available than ordinary legal-tender money. This will be accomplished by requiring every bank to receive on deposit certified checks on, or checks on ascertained deposits in, any other bank in the system, even though

such bank has suspended payments.[1] The clearing system that is to be introduced will quickly shift the burden of such payments from the individual banks to the banks as a whole.

But if the bankers are to suffer the losses arising from dishonest and inefficient banking, they should be given the power to prevent such banking. For this purpose a great part of the regulation of the

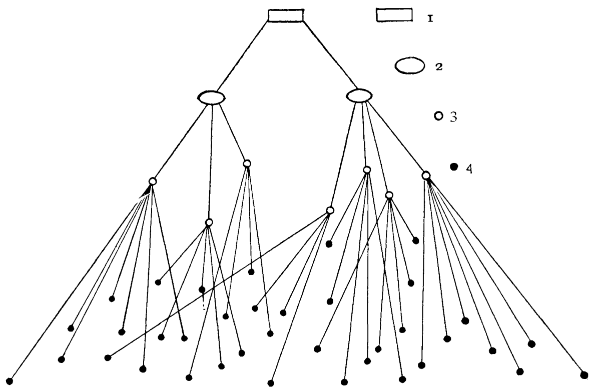

FIG. 1.

ILLUSTRATING THE ORGANIZATION OF DEMAND-DEPOSIT BANKS IN THE UNITED STATES.

1 United States Issue Department, administered by the Comptroller of the Currency.
2 District clearing houses.
3 Associations.
4 Banks.

banking business is entrusted to the banks. Every bank must belong to an association. The capital of the banks in each association must amount to at least 25 million dollars. The central office of the association must be in some city of more than 50,000 inhabitants. Each association must be a member of some district clearing house. There will be six or seven of these district clearing houses, located by law in the most important business centers. Each bank will have one vote in its association; each association one vote in its district clearing house.

[1] A bank will not be required to honor checks on such deposits to more than one-half the amount of its reserves till the deposited check has been cleared. The system of clearing to be introduced makes the time required for this purpose very short. Some officer of every bank, even though suspended, will be required to certify to deposits on request.

The association will regulate the business of banking among its banks, and its own administration subject to its district clearing house. The district clearing house will regulate matters common to all its associations and its own administration. The comptroller will have power to veto or revoke any regulation that grants special privileges to any bank or set of banks, and to decide controversies between district clearing houses and associations as to province of legislation. Upon petition of three district clearing houses the President will appoint a special commission of inquiry as to regulations cited in the petition, which will have power to revoke such regulations if they are found to operate unjustly to the special advantage of any bank or set of banks. The organization of banks and their entrance into associations will be so regulated by law that every community that can support a bank will have one, and that monopoly in the business will be an impossibility. Fig. 1 is intended to give a graphic representation of the organization of the banks. A glance will show that the banks in any association are not confined within territorial limits.[1]

The system of clearing will be regulated by law. Once every day each bank will send to its association all checks paid for other banks, and at the same time report the amounts of its reserve and deposits.[2] The association will credit each bank with checks received from it and charge it with its own checks received from other banks. At 12 M. each day the association will report to the banks their balances and any change in reserve requirements. In each association city there will be located a representative of all other associations, whose business it will be to receive checks paid for the banks of those associations and officially acknowledge the debit for their payment. This official acknowledgment will be made by attaching his signature to the report telegraphed by the local association at 12 M. each day to its district clearing house giving the amount of its payments for other associations. The association will also report the amounts of the reserves and deposits held by its banks. Each district clearing house will forward to the others the reports of payments made for their respective associations as fast as they are received. Such reported payments will be

[1] Banks may change their association if such change is acceptable to the Comptroller and to the association they wish to enter. An association can change its district clearing house under like conditions.

[2] It is expected that local clearings will be made before this report to the association.

cleared and the balances reported to the associations at 1 P. M., together with any new requirements as to reserves. They will at the same time report to the Issue Department net payments made for other districts and amounts of deposits and reserves in their own district. The Issue Department will clear these payments and report balances and new reserve requirements to district clearing houses at 2 P. M. All balances, less required reserves, will be subject to check the same as deposits. Fig. 2 illustrates the operation of such daily clearings among as few

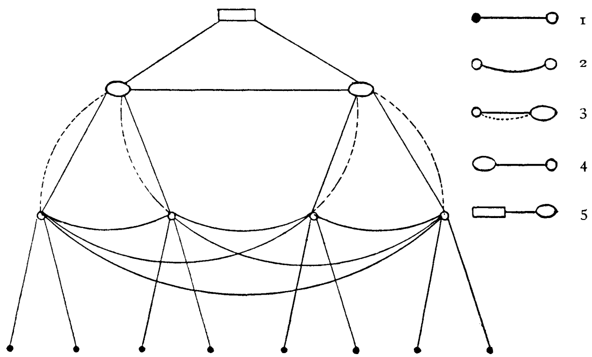

FIG. II.

ILLUSTRATING THE SYSTEM OF CLEARING.

1 Routes of checks and reports between banks and associations.

2 Routes of checks returned by association representatives.

3 Route of double telegraphic report from association representatives and associations to district clearing house.

4 Route of report from district clearing house to associations.

5 Route of reports between district clearing houses and issue department.

banks as could be organized under the proposed plan. The district clearing houses must keep on deposit in the Issue Department for the payment of balances at least 1 per cent. of all deposits in their respective districts. This requirement can be increased at any time by the comptroller.

The long accepted principle of uniformity of the currency will be adopted. Metals will not be used unless for small change. The currency will be restricted to the United States demand notes of the Issue Department. These will be a legal tender for all debts, public and private. All money, including gold and silver, now legal tender will

cease to be so. But United States coins and demand obligations of the United States will be redeemed by the Issue Department in United States demand notes, if presented before a designated date. These notes may also be obtained from the Issue Department in exchange for either gold or silver, without restriction as to quantity. The prices that are paid for these metals will vary in accordance with legal regulations.

In order to afford the country districts of the South and West as great credit facilities as are practicable, and to do away with the losses occasioned by crises and panics—so far as possible—the Issue Department will deposit demand notes with banks under certain conditions. If a bank wishes a deposit of notes from the Issue Department, it must deposit acceptable short time banking paper with its association. The association must then issue to the bank, association certificates up to 75 per cent. of the collateral accepted. On receiving these certificates as collateral, the Issue Department will deposit with the bank an equal amount of demand notes. While a bank's deposits bear a ratio to its capital less than 60 per cent. of the average ratio of deposits to capital throughout the system, the bank will pay the Issue Department 2 per cent. interest; while such ratio is between 60 and 80 per cent. of the average ratio, the rate will be 4 per cent.; while it is between 80 and 100 per cent. the rate will be 6 per cent. So long as the Issue Department has notes on deposit with the bank it will prevent such ratio rising above 100 per cent. by checking out the excess as fast as it appears. It is expected that these deposits will enable the small banks in the South and West, where the use of deposit currency is extremely limited, to afford their patrons nearly the same facilities for making payments that are enjoyed in the great financial centers of the North and East. The advantage of these deposits in a critical emergency may be illustrated by the following example. A bank holding a reserve of 25 per cent. has deposits that bear a ratio to its capital equal to such ratio throughout the system. Some very remarkable crisis makes it necessary for it to redeem all of its deposit liabilities within a few days. If its loans and discounts have been judiciously made the bank will, through this accommodation from the Issue Department, be able to meet such a drain without making a collection beyond what may be necessary to make up a possible excess of its reserves over its capital.

It is believed that in giving the legal-tender currency a basis that

is practically as broad as the combined stocks of gold and silver plus all the acceptable bank paper the country can furnish, this system offers to the debtor every protection against an appreciating standard that is now practicable; and that this, together with the extraordinary facility it affords for making payments in any section of the country, must satisfy the demands of every honorable advocate of debtors' rights.

II.

It remains to be seen whether these provisions can be enforced without doing injustice to the creditor, with a probable gain to the general credit of the country, and without conferring dangerous powers on any man or set of men. The first step in this direction will be the complete separation of the Issue Department from the fiscal administration of the government. The resources of the department and its power of issue will be as independent of control by Congress as those of any national bank at the present time. Through this department the comptroller will buy and sell gold, silver, and United States bonds, make such deposits in banks as have been indicated, and exercise supervision over the banking system. The Treasury will at once turn over to the Issue Department all money and bullion in its possession and receive for the same United States demand notes. The comptroller will then go on the market and buy or sell at the best prices in United States demand notes, a sufficient quantity of silver to make the stocks of the two metals held by him equal in value. The stock of silver will be estimated at the price at which the last purchase or sale is made. The gold will be stamped into ingots containing 2322 grains of pure gold, or 2580 grains of standard gold, the silver into ingots containing $25 worth of silver.[1] The size of the gold ingots will be permanent. The size of the silver ingots will not be changed till the end of a designated period of time, during which the abnormal effects of the initiation of the system, on the value of silver, will be expected to exhaust themselves. It will then be changed so that four ingots will contain $100 worth of silver at the department's selling price, and will remain unchanged thereafter. These gold and silver ingots will be sold in unlimited quantities to anyone offering demand notes for them. Until the change of silver ingots to their permanent size the selling price of the gold ingot will remain fixed at $100. The Issue Department will pay $99 in demand notes for the amount of gold in

[1] The same price will be used here as in estimating the stock.

an ingot.[1] Whenever the stocks of metal are equal in value[2] the prices of silver will be the same as those of gold. During the first period, in which the size of the silver ingot is only temporarily fixed, if the stock of silver is decreased in value by purchases of gold or sales of silver, to 49 per cent. of the whole stock, its purchase and sale prices will be raised to $100 and $101 respectively. A like increase in the prices will be made for each 1 per cent. of decrease in the stock of silver until its value is but 40 per cent. of that of the whole stock. Whenever the stock of silver increases the prices will fall, returning along the same road toward an equality with those of gold. Fig. 3

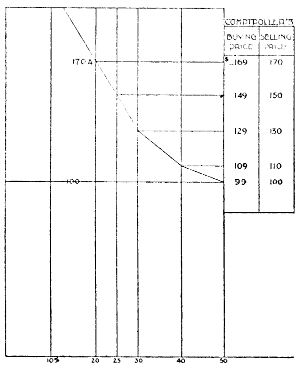

FIG. III.

SHOWING THE INCREASE IN THE ISSUE DEPARTMENT'S PRICES OF SILVER WHEN GOLD IS HELD IN EXCESS OF FIFTY PER CENT. OF THE TOTAL STOCK.

shows that whenever 40 per cent. of the total stock is in silver, its purchase and sale prices will be $109 and $110 respectively. While the silver stock is between 30 and 40 per cent. of the total stock, changes of a dollar in the prices will result from a change of one-half of 1 per cent. in the stock. The figure shows that as a result of such changes when the value of the silver stock stands at 30 per cent. of the total the prices will be $129 and $130. Thereafter the change in prices will be made for every change of one-fourth of 1 per cent. in

[1] This seigniorage charge of one dollar is made on purchases of ingots as well as bullion. There is no particular reason for fixing it at one dollar.

[2] The value of each stock will always be estimated at the price at which it is being sold.

the value of the stock of silver. The diagram shows that if silver appreciates in value 70 per cent. (to A), 20 per cent. of the Issue Department's stock will be in silver and 80 per cent. in gold.

If, however, the purchases of silver are in excess of those of gold, similar changes in its prices will be made in the opposite direction. Fig. 4 shows that when the silver stock stands at 60 per cent. of the total stock, its prices will be $89 and $90; that at 70 per cent. its prices will be $69 and $70; and that if it depreciates in value one-half it will constitute three-fourths of the entire stock. After the silver ingots are changed to their permanent size, an excess in the stock of gold, instead of raising the price of silver, will cause a like decline in its own prices. Under these regulations the selling price of either metal can never exceed $100.

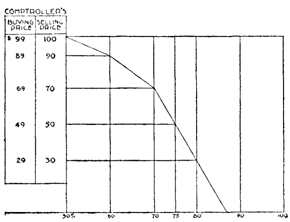

FIG. IV.

SHOWING THE DECREASE IN THE ISSUE DEPARTMENT'S PRICES FOR EITHER METAL THAT IS HELD IN EXCESS OF FIFTY PER CENT. OF ITS WHOLE STOCK.

What would be the result of this unlimited purchase and sale of gold and silver by the Issue Department? It would be bimetallism, but not the old bimetallism. We have here the same liberty to use both metals. We have also the same resort to the alternative standard. Here the likeness ceases. In the old bimetallism the metal relatively depreciating in value always fixes the standard and its depreciation is retarded by the decreased use of the other metal. In the new bimetallism the metal relatively appreciating fixes the standard, and its appreciation is retarded by an increased use of the other metal. Under the old bimetallism the appreciation in the value of a metal often drives it entirely out of circulation. Under the new, every pound of gold and silver bullion in the country will always be available as money. The founders of our government believed that the currency

should be based on both metals; they also wished that the metals might be used at the market ratio. The new bimetallism gives the currency the bimetallic basis and provides for the use of the two metals at that ratio. Under the old bimetallism the change from one standard to the other occurred only at long intervals. Under the new, because of the use of the metals at the market ratio, the two standards may be in use on the same day. Under the old bimetallism the standard is sometimes lower than that of silver standard countries, and at all other times lower than that of gold standard countries. Under the new, the standard may at times be higher than that of some other countries, but never can be lower than that of any. Under the old bimetallism a given quantity of one of the metals determines the value of the dollar, and the whole demand for monetary metal centers upon the supply of that metal. Under the new, the constantly fluctuating metal equivalent of the dollar allows both metals to compete at all times in supplying the demand for monetary metal. It is generally admitted that increased sources of supply decrease variations in value. The threatened adoption of the old bimetallism creates a panic in the commercial world. The adoption of the new would secure to the creditor payment in the best money in the world, whether that be gold or silver.

Theoretical benefits to the creditor, however, will count for nothing if there can be any question of the comptroller's ability to supply demands for either metal whenever made. Those provisions of the system intended to enable him to do this will next be considered.

He will be required to maintain the same ratio between his stock of gold and silver and the demand notes in circulation as the banks maintain between their reserves and deposits. As the changes in the metal stock are not subject to his own control it follows that he must have the power to vary the amount of notes outstanding in accordance with such changes. He is enabled to do this through his control of the amount of their reserve which the district clearing houses are required to keep on deposit in the Issue Department, and by the purchase and sale of United States bonds. If the district clearing house reports show an increase in the bank reserves, while on the same day the Issue Department's transactions in gold and silver indicate, by decreasing the ratio of the gold and silver stock to the amount of notes outstanding, a depreciation in the value of the demand notes, this increase in the bank reserves will be assumed to be the result of contractions

in loans and discounts by the more prudent bankers, and a like contraction throughout the entire system will be enforced by requiring an increased deposit of reserves in the Issue Department. This increased requirement will express itself in a draft on the district clearing houses for an amount of demand notes sufficient to contract the circulation outstanding to the required ratio with the Issue Department's stock of metal. Any depreciation in the value of demand notes, from whatever cause, expressing itself in a run on the Issue Department's metal stock,[1] will always be met by a similar contraction of the amount outstanding by increasing the reserve deposit. For instance, if the bank reserves stand at 25 per cent. and the excess of the comptroller's sales over his purchases is one million dollars, he will draw on the district clearing houses for three millions. If the reserve is standing at 20 per cent. he will draw for four millions.[2] It will be seen at once that an unreasonably low reserve held by the banks will cause these drafts to become disagreeably large. If the reports show the comptroller's reserve to be excessive, the reserve deposit requirement will at once be reduced, and notes from that deposit will be returned to the district clearing houses in sufficient amounts to restore the equilibrium by expanding the circulation. But if the district clearing house deposit with the Issue Department is at the 1 per cent. limit, the comptroller will go on the market and buy United States bonds to expand the circulation to the required amount. If there are no United States bonds to be bought on the market or if the holders of such bonds charge a premium that indicates a market demand for United States bonds bearing interest at a rate more than one-half of 1 per cent. lower than any at that time on the market, the Secretary of the Treasury will issue bonds bearing the indicated rate, and sell the comptroller a sufficient quantity to produce the required expansion of the currency. This expansion will not be so immediately operative as those through the return of the reserve deposit, or through buying bonds from the public, but it is not to be expected that there would be many resorts to it. If at any time that part of the bank's reserves held by the comptroller amounts to 10 per cent. of their deposits, he shall thereafter draw on the district clearing houses for only one-half the required contraction, and shall obtain the other half by the sale of United States bonds. Whenever his own

[1] This may sometimes be caused by the deposit of notes with the individual banks.

[2] It is hardly necessary to state that these drafts will be in proportion to the deposits held by the different districts.

stock of bonds is exhausted, the Secretary of the Treasury shall issue new bonds to him in exchange for demand notes in any amount that he may need for maintaining the required ratio between the notes outstanding and his stock of gold and silver.

To get a clear idea of this system of issuing notes and keeping them at par with the standard let us look upon the Issue Department as an independent bank of issue. It can get its notes into circulation only by buying gold and silver and bonds of the United States on which it will receive no interest, and by making deposits in banks under certain conditions. The amount of its issues in excess of purchases of gold and silver is limited by the amount of the deposit liabilities of the banks in excess of their reserves. It follows that the issue of notes cannot become excessive except through an excess of bank loans and discounts. But if the banks raise general prices by unwarranted discounting, so that large imports and a demand for gold or silver for export are occasioned, they are at once reminded of their folly by the increased deposit of reserve required by the comptroller.[1] The justice of this increase in the requirement is evident, as it will never be made except as the result of their own indiscretion in expanding the deposit-currency. Since the banks alone can occasion an inroad upon the comptroller's stock of gold and silver, it is but right to place their assets, to the measure of their deposits, at his disposal for the purpose of stopping any such inroad.

The requirement that the United States government shall place its entire resources at the comptroller's disposal for the same purpose cannot be justified on quite the same grounds. It is true, however, that it is almost impossible to conceive of too great expansion of the note issue, except through the purchase of United States bonds, and the saving of interest to the United States that results from these purchases calls for some return. Moreover, the fact that the general interest of the country demands a confidence that can be established only by such absolute guarantee of the stability of its standard of value is sufficient reason for granting him this sure resource to which, in all probability, he will never be compelled to resort. Do not these provisions enable us to say to the creditor: "In no country in the world is the standard of deferred payments so securely guarded against depreciation as in the United States?"

[1] The seignorage charge of $1 will prevent any sales of metal for export by the Issue Department, except when the demand notes are depreciated.

III.

While making these provisions for the debtor and creditor, has anything been accomplished for the interests of the country as a whole? It is hoped that a monetary policy has been proposed that will meet the demands of the gold man, the silver man, and the government-currency man. This will mean a stable monetary policy, which will bring with it advantages to every class and every individual in the nation. The fiscal administration of the government will no longer attempt to do a banking business, and anyone can tell when bonds are issued to make good a deficit and when to redeem government currency. It is believed that the specter of inflation will be laid once for all. Could an emergency arise that would tempt Congress to an abnormal issue of paper money when it knows that the country is constantly using its demand credit as freely as the wisdom of the bankers will allow them to use theirs, and when it will have been educated by seeing the circulation contracted from time to time because of its depreciation through overissue? Nevertheless, the country as a whole will reap what profit arises from the economy of substituting a paper currency for one of metal. The advantages that will be derived from the increased mobility of capital cannot be confined to any class. The device that enables the comptroller to relieve a financial pressure, or stop a panic at some particular point, and if such operation unduly expands his issues, to contract them by a draft upon the whole banking system, may seem local in its benefits, but the business life of the nation is so organic in its nature that to cure a local ailment is to strengthen the whole system. The security that it would afford to the millions who must intrust their money to the care of others does not seem a small thing to one who has watched the suffering caused by bank failures. But the benefits derived from this security is not confined to the depositors. The hoards of the distrustful will become active capital. The fact that the failure of a bank cannot lock up a dollar of capital will alone be a great benefit.

To sum up, in conclusion, a few of the reasons for expecting such a policy to receive popular support: It gives the creditor a greater measure of security than he has ever yet known; it does even more for the debtor than for the creditor; it provides for the unlimited use of both gold and silver as monetary metals; it gives to the country all the profit that can be derived from substituting a paper currency for

one of metal; it insures for bank depositors the immediate availability, under any emergency, of every cent of their deposits; it frees our banking system from the constant fear of regulations enacted by men entirely ignorant of the banking business, and will undoubtedly increase very much the amount of their deposits and the limit to which they can safely carry their loans and discounts; it provides means for securing a note circulation for those sections of the country that are not able to make use of a deposit currency; it brings without delay the great financial resources of the nation to the support of any section that is suffering from a monetary stringency, and in doing this renders the whole system so sensitive to credit excesses that it is hoped the worst effects of great crises may be altogether avoided.

WORTHY P. STERNS.

UNIVERSITY OF CHICAGO.